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REVIEW GUIDE

FOR

FEDERAL AGENCY

ACCOUNTING SYSTEM DESIGNS

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REVIEW GUIDE FOR FEDERAL AGENCY

ACCOUNTING SYSTEM DESIGNS

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## SECTION 1

### INTRODUCTION

This review guide is designed to be used by:

- staffs of Federal agencies in developing their accounting system designs to the point where approval by the Comptroller General can be requested,
- staffs of Federal agencies in developing the documentation of an accounting system being submitted for approval by the Comptroller General, and
- the GAO Financial Management Staff to systematically consider and review designs of accounting systems submitted by executive agencies for approval by the Comptroller General.

Additional review guides have been developed for use in evaluating (1) payroll and (2) ADP aspects of an accounting system design. If the system being submitted is both automated and integrated, all three review guides should be submitted. If not, the agency should submit the review guide(s) that apply to all aspects of the system design being submitted for review. (A separate review guide has also been prepared for use in evaluating statements of accounting principles and standards.) This review guide does not include specific questions on the various facets of a separate payroll system relating to processing and control of payroll data. In some cases it may, therefore, be necessary to use an agency's completed payroll system review guide in conjunction with this review guide.

### CONCEPT AND COMPOSITION

The review guide is based on the concept that the reports will be reviewed first, the account structure second, and the accounting processes last. This is a logical review sequence in that (1) the financial information needed to prepare the agency's reports must be

identified before the account structure can be evaluated and (2) the accounts to be maintained must be identified and their contents described before the accounting processes can be evaluated. The review guide is, therefore, divided into sections which correspond with this approach. That is, some sections are concerned solely with financial reporting requirements, some with the prescribed account structure and others with the various accounting processes. Each of these sections includes five parts:

1. The "Objectives" part of each section sets forth broadly stated objectives which that portion of the review is to accomplish and is intended to provide the reviewer with a general goal toward which he should work.

2. The "Applicable Principles and Standards" part of each section delineates the accounting principles and standards that are prescribed by the Comptroller General and that the accounting system design must comply with.

3. The "Discussion" part of each section brings out certain additional information and explanation relating to GAO requirements that would be useful to the reviewer during his evaluation, and to an agency in developing documentation, but that is not specifically stated in the Comptroller General's accounting principles and standards.

4. The "Check List" part of each section presents selected questions to be answered by the agency and to be cross-referenced to the design documentation. (Further discussion of this area is presented on page 1-3).

5. The "Summary" part of each section provides an outline for briefly describing the results of the review and is intended to facilitate and expedite preparation of the required summary report by the GAO reviewer. It need not be of concern to agencies in developing and providing references to their design documentation.

#### REFERENCES

Notations that appear in parenthesis at the end of the principles and standards and at the end of the check list questions are references to applicable sections in Title 2 of the GAO Manual for Guidance of Federal Agencies.

Notations that appear in parenthesis in the summary part of each section are references to a GAO Financial Management Staff internal memorandum which provides guidelines to GAO reviewers for preparing a required internal summary report upon completion of the review.

#### CHECK LISTS

Some of the questions included in the "Check List" parts of the review guide are similar in nature. For example, most of the sections relating to accounting processes ask whether the design includes a description of the general ledger accounts to be maintained. Although this appears to represent numerous duplications, it should be kept in mind that the check lists are intended as a tool to aid the reviewer in identifying those portions of the design documentation upon which to base his evaluation as to whether the system design conforms to the principles and standards included in each section.

The check lists are also intended to assist in assuring that the design documentation includes the necessary elements. In completing the check list parts, the agencies may prefer to provide one overall reference (or a series of references) to answer similar questions. In order to avoid unnecessary effort and/or misinterpretation of the check list questions, it is recommended that agencies consult with GAO staff members when completing the check lists.

#### APPLICABILITY

The review guide covers the accounting principles and standards prescribed by the Comptroller General. However, some systems submitted for approval may not involve all such principles and standards. Therefore, in reviewing a particular system design some adjustment to the review guide may be necessary.

Prior to assembling the documentation for a system design being submitted for GAO's approval, Federal agencies should identify the principles and standards and the check list questions which are not applicable to the system design. In such cases the check list questions should be so indicated with the words "not applicable" (N/A). Likewise, before starting to review an accounting system design, the reviewer should identify the principles and standards and the check list questions which are not applicable to the design being reviewed.

#### FEDERAL AGENCY'S RESPONSES

A positive answer to any of the check list questions should be followed by a reference to the pertinent part of the agency's submission

(by page and paragraph number) which demonstrates how the system design or the design documentation relates to the question asked.

A negative answer or an answer of "not applicable" should include a reference to a statement in the agency's submission which explains the reason or justification for such a response. The reviewer should be alert to the possibility that such answers may indicate a deviation from a prescribed principle or standard.

#### ADVANTAGES

Use of the review guide in reviewing accounting system designs is intended to provide the following advantages.

1. Contribute to the completeness of the review in that it requires analysis of the design in relation to particular principles and standards.
2. Contribute to the efficiency of the review in that related principles and standards are grouped and each group is to be reviewed in a logical sequence.
3. Ensure that a consistent approach will be followed in reviewing each system design.



## SECTION 2

### STATUTORY REQUIREMENTS, RELATIONSHIP TO OTHER SYSTEMS, AND

#### RELATIONSHIP TO OTHER FINANCIAL MANAGEMENT FUNCTIONS

##### OBJECTIVES

Our primary objectives are to indentify:

- statutory requirements specifically applicable to the accounting system under review (or to the activities which it supports),
- the relationship of the accounting system to other financial management functions,
- the interface of the accounting system with other related systems, and
- the agency's plans for implementation of the design.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Statutory requirements

An agency must comply with the provisions of all applicable laws relating to agency accounting and to the administration of the funds and appropriations for which it is responsible. (Sec. 8.1)

###### Relationship to other financial management functions

The accounting system of each agency shall be designed to meet all internal needs for cost and other financial data for planning, programming, budgeting, control and reporting of agency operations. (Sec. 8.2)

To the extent possible, planning, programming, budgeting and accounting classifications shall be consistent with each other and should be synchronized with the agency's organizational structure. (Sec. 8.6)

###### Interface with other systems

No specific principles and standards are prescribed.

###### Implementation plans

No specific principles and standards are prescribed.

## DISCUSSION

If the accounting system design is to produce inputs to other systems, the data requirements of the other system will be considered only to the extent necessary to verify that the accounting system design will satisfy these requirements. If the accounting system design is to receive inputs from other systems, the controls contained in those systems will be examined only to the extent necessary to insure timely and accurate transmission of the data to the accounting system being reviewed.

The determination as to whether the other systems are so designed as to satisfactorily produce information to satisfy the requirements of the accounting system being reviewed is a function of the design review of the interfacing systems. If the interfacing systems are not accounting systems they are not subject to our approval, but they may be reviewed by GAO as an audit function.

Part of our objective in this section is to identify any specific statutory requirements applicable to the accounting system (or activity) under review. For example, a working capital fund, industrial fund, etc., for which an accounting system is being evaluated is usually governed by a specific statute. Therefore, the reviewer must be aware of the requirements contained in such statutes and must determine, during his subsequent evaluation of the system, whether the system complies with these requirements.

Section 27.5 1.a to 1.d of Title 2 sets forth design documentation requirements relating to a general description of the accounting system, including the relationship of the accounting system to the agency's program, budget and organizational structure and the interface of the accounting system with other systems. Section 27.5 8.a and 8.b of Title 2 sets forth design documentation requirements relating to the plans for implementing the accounting system. The following questions are generally related to these requirements.

## CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design documentation include references to, or cite sections of, pertinent provisions of law applicable to the accounting system?	_____	_____

	<u>Answer</u>	<u>Reference</u>
2. Does the design show the agency's decision as to the organizational levels for which budgeting and accounting data will be accumulated?	_____	_____
3. Does the design show:		
a. the program structure which will be used for budgeting and accounting?	_____	_____
b. the extent that data can be directly charged to programs and/or the extent that allocations or cost-finding techniques will be used?	_____	_____
4. Does the design show:		
a. how financial data will be classified in the accounting system to permit accumulation of data necessary to accommodate the budget structure used for presentation of the budget requests to the Congress, including the subordinate project statements?	_____	_____
b. the extent that financial data can be classified directly to budget activities and subactivities and/or the extent that allocations will be made?	_____	_____
5. Does the design explain the system of planning used by the agency and indicate how the structure used in the accounting system will support the planning structure?	_____	_____
6. Does the design show how the system will interface with other related systems?	_____	_____
7. Is the accounting system designed to provide the required inputs to the related system?	_____	_____
a. Are the data requirements of the related system described?	_____	_____
8. Is the accounting system designed to receive outputs from interfacing systems?	_____	_____
a. Are controls contained in the interfacing system for providing timely and accurate transmission of data described?	_____	_____
9. Does the design include charts which show the flow of data to and from related systems?	_____	_____

	<u>Answer</u>	<u>Reference</u>
10. Does the design documentation include:		
a. for those systems in the developmental stages:		
(1) a schedule (milestones) for the development of procedures and manuals needed to implement the accounting system design?	_____	_____
(2) the proposed conversion process including plans for training?	_____	_____
(3) a tentative schedule for implementing the system (testing and development milestones up to and including initial implementation and declaration of the system operational)?	_____	_____
(4) a description of the planned methods for testing the logic and reliability of the system?	_____	_____
(5) provisions for evaluating system test results and making appropriate adjustments to the system design to prevent problems identified from reoccurring?	_____	_____
b. for those systems implemented and declared operational:		
(1) provision for testing the logic and reliability of changes to the system?	_____	_____
(2) provision for evaluating sytem change tests prior to implementation of the changes in an operational mode?	_____	_____

#### SUMMARY

Briefly describe the relationship of the system to any other accounting systems of the agency and to the agency's overall financial management system. ( 2/19/75 Memo, Item B (4))

Briefly indicate the extent to which the system is integrated or interfaced with other financial management functions of the agency. (2/19/75 Memo, Item B (5))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

### SECTION 3

#### FINANCIAL REPORTING

##### REPORTS TO BE PREPARED

##### OBJECTIVES

Our primary objectives are to:

- identify the internal and external reports,
- ensure that the agency plans to prepare the prescribed financial reports, and
- ensure that the agency plans to prepare other reports designed to meet all internal needs for cost and other data.

##### APPLICABLE PRINCIPLES AND STANDARDS

The accounting system shall be designed to meet all internal needs for cost and other financial data for planning, programming, budgeting, control, and reporting of agency operations. (Sec. 8.2)

The financial data produced by the accounting system must be useful to the officials requiring it. (Sec. 8.4)

Agencies financed from appropriations or similar authorizations should prepare periodic reports on the status of such authorization as prescribed by OMB. (Sec. 17.2(d))

Special financial reports required by the Congress, its committees, and the central agencies should be prepared in accordance with prescribed instructions. (Sec. 17.2(f))

Financial reports to be prepared include:

1. External reports required by control agencies and others.
2. Internal reports useful to agency management.  
Basic internal reports required will be (1) statements of assets and liabilities and (2) statements of operations of an agency's programs and activities.  
(Sec. 17.2)

Financial performance in relation to statutory or other limitations prescribed by higher authority shall be specifically reported. (Sec. 17.3(a)(7))

Separate statements should be prepared for each fund. Combined or consolidated statements for two or more funds should be prepared if such statements will better present the financial operation or condition of the agency. (Sec. 17.2(e))

#### DISCUSSION

In essence, the agency should:

- provide an appropriate recurring report to each manager/ activity within the agency who has a legitimate need for financial information,
- prepare all applicable reports prescribed by external organizations, and
- prepare financial reports prescribed in Section 17.2 of Title 2.

Reports required of and prepared by each agency will necessarily vary with the purpose to be served. All accounting systems are required to prepare some of the reports prescribed in Title 2; e.g., Statement of Assets and Liabilities. However, the type of operation to be accounted for may be such that all reports may not be applicable to the accounting system under review. For example, reports prepared for an operation financed through an appropriation would be different than those prepared for activities involved in a business-type operation (and vice versa). The data required for external reports will ordinarily call for less detailed information, perhaps reported less frequently, than the data needed by the agency for its own internal reports. Both external and internal reports should ordinarily be prepared from the same source data and should be in agreement.

All reports to be prepared by the agency should be identified early in the review so that the data needed for their preparation may be considered when we determine whether the accounting system is capable of providing all needed financial information.

#### CHECK LIST

- |   | <u>Answer</u> | <u>Reference</u> |
|---|---------------|------------------|
| 1. Is there a description for each internal recurring report, including the title, form number, purpose, frequency, period covered or "as of" date? (Sec. 27.5 2.b) | _____         | _____            |
| 2. Is there a listing by title and form number of external reports produced or partially produced by the system? (Sec. 27.5 2.d)                                    | _____         | _____            |

	<u>Answer</u>	<u>Reference</u>
3. Will the reports prescribed by Sec. 17.2 be prepared by the agency?		
a. does the design specifically identify which of these reports will not be prepared?	_____	_____
b. does the design provide a justification or basis for not preparing a particular report?	_____	_____

SUMMARY

Describe briefly the basic types of reports to be produced by the  
agency. (2/19/75 Memo, Item C (1) (k))

Comments on any problem areas noted. ( 2/19/75 Memo, Item D)



## SECTION 4

### FINANCIAL REPORTING

#### ADEQUACY OF REPORTS

#### OBJECTIVES

Our primary objectives are to:

- determine whether the financial reports proposed by the agency will provide a clear and complete disclosure, and
- ensure that the agency intends to include the prescribed cost information in its reports and financial statements, when appropriate, and ~~that~~ cost information is adequate for the purpose for which it is to be used.

#### APPLICABLE PRINCIPLES AND STANDARDS

##### Adequacy of financial statements

Financial reports should be prepared to clearly disclose significant financial facts about agency operations and activities. (Sec. 17.1)

Specially ~~designed~~ additional reports should be prepared to round out each agency's pattern of financial reporting to fully disclose the financial aspects of its operations. (Sec. 17.2(f))

The amount of detailed information shown, including explanatory notes as to unusual items, graphic presentations where appropriate, and accompanying interpretative comment shall be sufficient to provide a clear and complete report. However, unnecessary detail shall be avoided particularly where the effect of its inclusion would be to obscure significant financial data. (Sec. 17.3(a)(6))

The effect of all transactions occurring during an accounting period shall be included in the financial reports for that period. (Sec. 8.10(b))

### Adequacy of cost reports

An accounting system must provide a basis for reporting costs of performance in accordance with:

- a. Major organizational segments,
- b. Budget activities, and
- c. Program structure. (Sec. 8.2)

Agency accounting systems must produce appropriate data on the cost of carrying out operations. (Sec. 16.3)

Needed cost information will be produced for management and reporting purposes. (Sec. 16.4)

Adequate cost reports are required in support of:

- a. implementation of cost-based budgets,
- b. the requirement to account for costs where reimbursement for services performed is to be at cost or where sales prices are primarily based on cost, and
- c. the requirement to account for costs where full recovery of cost from customers or users of services is a statutory requirement. (Sec. 16.4)

Cost accounting techniques should include, where appropriate and feasible, the production of quantity data related to performance or output. (Sec. 16.4)

Cost reports by area of responsibility should be consistent with the assignment of responsibility. (Sec. 16.4(3))

### DISCUSSION

The agency must prepare financial reports which clearly and completely disclose the important financial aspects of the agency's operations.

A discussion of costs to be included in cost reports is included in Section 15--Accounting for Costs.

Reporting standards are discussed in detail in Section 17.3 of Title 2. The reviewer must consider whether the reports to be prepared by the agency comply with those standards. Adequacy of fund control reports is included in Section 6 of this review guide.

### CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Are the types of financial information to be provided the various levels of management <u>on</u> internal reports described? (Sec. 27.5 2.c(1))	_____	_____
2. If the agency plans to produce any financial data or reports based on sources other than the accounting system, does the design explain the basis <u>used</u> for determining such data? (Sec. 17.3(a)(3))	_____	_____
3. Will internal reports be prepared which compare actual with planned costs?	_____	_____
4. For revenue-producing operations, will reports be prepared which compare revenues earned with the cost of providing the related service or product? (Sec. 17.2(b))	_____	_____
5. Do internal reports provide information on unit costs?	_____	_____
6. Do the cost reports include and identify indirect and unfunded costs where full cost is required?	_____	_____

### SUMMARY

Comment on any problem areas noted (2/19/75 Memo, Item D)

## SECTION 5

### FINANCIAL REPORTING

#### REPORT QUALITIES

##### OBJECTIVES

Our primary objectives are to ensure that the agency has:

- adopted an appropriate pattern of reporting for each type of recurring internal report (e.g., fund status, status of internal cost-based budgets, costs, etc.),
- established an appropriate issuance date for each report and an appropriate reporting frequency for each internal report, and
- given appropriate consideration to prescribed requirements when establishing formats for and information to be included in the reports and statements that it plans to produce.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Internal Reporting Pattern

The basic pattern followed in the preparation and submission of internal financial reports should be in conformity with assignments of responsibility to organizational units. (Sec. 17.3(d))

###### Timeliness

Financial data must be promptly presented. (Sec. 8.4)

Financial reports should be prepared and issued as often as necessary to be of maximum use to management officials and to meet prescribed external requirements. (Sec. 17.1)

Generally, reports should be prepared to cover--or be issued at the end of--accounting periods of four weeks or a calendar month. (Sec. 17.1)

All needed reports must be produced promptly to be of maximum usefulness. The issuance of reports should not be delayed, and the cost and effort should not be incurred to produce relatively minor refinements of data. (Sec. 17.3(c))

Financial reports prepared by Federal agencies must comply with the specific requirements of applicable laws and regulations as to frequency. (Sec. 17.3(b))

### Requirements for all reports

All essential financial facts relating to the scope and purpose of each report and the period of time involved shall be included and clearly displayed. (Sec. 17.3(a)(1))

The financial data reported shall be derived from accounts that are maintained on a consistent basis from period to period; material changes in accounting policies or methods and their effect shall be clearly explained. (Sec. 17.3(a)(8))

All appropriate steps should be taken to avoid bias, obscurement of significant facts, and presentation of misleading information. (Sec. 17.3(a)(2))

Where financial data or reports based on sources other than the accounting system are presented, their basis should be clearly explained. (Sec. 17.3(a)(3))

Consistent and nontechnical terminology shall be used in financial reports to promote clarity and usefulness. (Sec. 17.3(a)(9))

Financial reports prepared by Federal agencies must comply with the specific requirements of applicable laws and regulations as to nature and content. (Sec. 17.3(b))

Financial reports prepared by Federal agencies must comply with all applicable restrictions pertaining to information that is classified for national security purposes. (Sec. 17.3(b))

### Requirements for Financial Reports

Interagency and interfund transactions should be separately identified in agency records and statements so that they may be properly treated in preparing consolidated financial statements. (Sec. 8.7)

When foreign currency is not readily convertible to U.S. currency reports may be stated in dollar terms but the reports should disclose that the dollar amounts shown for foreign currency transactions and balances do not represent revenues, expenditures and assets in terms of realizable U.S. currency. (Sec. 12.3)

Estimates of the portion of accounts receivable that may not be collectible shall be disclosed separately in financial reports. (Sec. 12.4(6))

Receivables collectible in a form of foreign currency and not freely convertible may be stated in dollar terms using the appropriate conversion rate if the report contains a statement disclosing that the balance of such receivables are not assets in terms of realizable U.S. currency. (Sec. 12.4(7))

Significant classifications of property should be established for reporting purposes to clearly disclose the nature of the property. (Sec. 12.5(c))

Loans authorized but not disbursed should be disclosed in explanatory notes to financial reports. (Sec. 12.4(4))

The financial statements or notes thereto should contain a general description of the method(s) use in computing depreciation of major classes of depreciable assets. (Sec. 12.5(h))

Extraordinary items of revenue and cost shall be shown separately from the results of ordinary items in the statements of operations. (Sec. 14.6)

Contingent liabilities of material amounts shall be disclosed and explained in the financial reports. (Sec. 13.3)

Financial reports on Federal insurance, pension, and similar programs which are measured on an actuarial basis shall disclose the full current costs of these programs as they accrue and the estimated liability at any given time to make future payments. (Sec. 13.4)

The major elements of the Federal investment shall be separately disclosed in financial reports. Major changes for each fiscal period should be summarized in separate financial schedules. (Sec. 14.1)

Agencies shall disclose in financial reports the cost and related liability for accrued annual leave as of the close of each fiscal year as a minimum. (Sec. 16.8(a))

Costs incurred and paid by other agencies should be separately identified in agency financial reports. (Sec. 16.8(d))

All realized gains or losses on exchange transactions shall be disclosed in financial reports. (Sec. 16.8(f))

Unusual costs or losses of a nonrecurring nature which are substantial in amount should be classified separately in operating statements. (Sec. 16.8(g))

If significant amounts of costs applicable to an activity for which a statement of operations is being presented are excluded by reason of their being financed by other agencies or funds, such exclusions shall be clearly explained in accompanying notes along with estimates of the amounts involved. (Sec. 17.3(a)(4))

Net increases or decreases in the liability for annual leave should be classified as an operating cost for the year, at least at the appropriation level, in agency financial reports. (Sec. 16.8(a))

#### Requirements for Internal Reports

Financial data must be clearly reported and its significance readily understandable. (Sec. 8.4)

The form, content, and arrangement of each report shall be as simple as possible and designed to communicate significant financial information clearly to the users of the report. (Sec. 17.3(a)(5))

The preparation and distribution of reports that are unnecessary, not useful, or excessively detailed should be avoided as causing an unnecessary expenditure of public funds. (Sec. 17.3(d))

#### Requirements for Cost Reports

Cost reports should disclose the nature and estimated amount of any significant elements of cost omitted from the accounting system and the reason for the omission. (Sec. 16.4(1))

Accounting practices for allocating indirect costs must be devised with care so as to avoid producing cost data that obscures the total costs for which responsible managers should be held accountable. (Sec. 16.4(3))

Costs assigned to a given organization or purpose should include estimates of costs paid or financed through other funds or agencies. (Sec. 16.4(4))

Unless specifically required by law, forms of leave other than annual leave need not be recorded unless complete cost information is required. (Sec. 16.8(a))

Depreciation must be included in cost reports in specific circumstances. (Sec. 16.8(b))

Accounting procedures should be adopted by each agency to incorporate costs incurred and paid by other agencies into its accounting system whenever periodic determinations of total costs of performance are needed and the amounts of the costs incurred and paid by other agencies are determined to be of significance in relation to the total costs of the agency, activity, or operation on which financial reports are being prepared. (Sec. 16.8(d))

Losses which have been actually incurred or which may be reasonably expected to occur during the accounting period shall be disclosed in financial reports. (Sec. 16.8(f))

#### DISCUSSION

The above principles and standards establish requirements applicable to each report and financial statement to be prepared by the agency. In addition, they require certain information to be included in the agencies' financial statements and prescribe the manner in which some information is to be presented.

Each report must be prepared promptly and as frequently as necessary. All reports prepared by the agency for internal use must be necessary and financial data must be clearly reported.

Agencies are required to (1) identify all costs omitted from cost reports, (2) design reports so that costs of primary interest to recipients are not obscured, and (3) include certain elements of costs in cost reports under specified circumstances.



As a general rule, the elements of costs to be included in a cost report should be determined on the basis of the needs of the recipients. When full costs are required, however, all indirect costs, unfunded costs, and cost incurred and paid by other agencies should be included.

2 GAO 12.3 discusses financial statement disclosure of foreign currencies in excess of the needs of Treasury which have been allocated to agencies for use in their programs.

<u>CHECK LIST</u>	<u>Answer</u>	<u>Reference</u>
1. Is there a description, supported by a chart, of the overall recurrent reporting plan of the entity (e.g., pyramidal reporting) in regard to both: (a) its internal operations, including lower management echelons, and (b) external reporting responsibilities? (Sec. 27.5 2.a)	_____	_____
2. Is a sample format for each internal report included, showing illustrative data elements (column headings and stub captions), with pro-forma data inserted? (Sec. 27.5 2.c(2))	_____	_____
3. What is the accounting period (i.e., calendar month, 4 weeks, etc.) for which data will be accumulated and reported?	_____	_____
4. Does the design documentation demonstrate that financial reports will be produced promptly?	_____	_____
5. Will internal financial reports conform to assignments of responsibility to organizational units?	_____	_____
6. Will reports that are produced be consistent from period to period?	_____	_____

	<u>Answer</u>	<u>Reference</u>
7. If financial data is presented which is based on sources other than the accounting system will such sources be clearly explained?	_____	_____
8. Will interagency and interfund transactions be separately identified in financial reports so that they may be properly treated in preparing consolidated financial statements? (Sec. 8.2)	_____	_____
9. Will foreign currency transactions ever be included in financial statements?	_____	_____
10. Will explanatory notes be included in financial statements?	_____	_____
a. If so, does the design documentation indicate the type of information that will be included in them?	_____	_____
11. If the agency's operations involve programs which are measured on an actuarial basis, will financial reports disclose:		
a. the full and current cost of these programs as they accrue?	_____	_____
b. the estimated liability at any given time to make future payments?	_____	_____
12. Will financial reports prepared by the agency comply with applicable laws and regulations as to:		
a. frequency?	_____	_____
b. nature?	_____	_____
c. content?	_____	_____
d. information that is classified for national security purposes?	_____	_____

	<u>Answer</u>	<u>Reference</u>
13. Will the following be recognized in financial reports:		
a. realized gains and losses on exchange transactions?	_____	_____
b. unusual costs or losses of a nonrecurring nature? (i.e., extraordinary items)	_____	_____
c. losses (other than <del>on</del> exchange transactions) which have been actually incurred during the accounting period?	_____	_____
d. losses which may be reasonably expected to occur at a future time?	_____	_____
e. depreciation?	_____	_____
f. amounts of uncollectible accounts receivable?	_____	_____
g. costs incurred and paid by other agencies or funds?	_____	_____
h. contingent liabilities?	_____	_____
i. significant classifications of property?	_____	_____
j. major elements of the Federal investment?	_____	_____
k. cost and related liability of accrued annual leave?	_____	_____
l. extraordinary items of revenue?	_____	_____

#### SUMMARY

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 6

### FINANCIAL REPORTING

#### FUND CONTROL REPORTS

#### OBJECTIVES

Our primary objectives are to insure the agency plans to:

--Provide appropriate reports on status of funds to:

1. the agency head or his designated fund coordinator.
2. the budget office.
3. allottees and recipients of other administrative subdivisions made for the purpose of restricting obligations to authorized amounts.

--Issue fund status reports promptly and at appropriate intervals.

--Prevent the maintenance of unnecessary cuff records for apportionment control purposes.

#### APPLICABLE PRINCIPLES AND STANDARDS

##### Timeliness of fund control reports

Obligation information must be reported promptly.  
(Sec. 10.4)

##### Accuracy of fund control reports

Obligation information must be reported accurately.  
(Sec. 10.4)

Only those amounts meeting the criteria of section 1311 of the Supplemental Appropriation Act, 1955 (31 U.S.C. 200), will be reported as obligations. (Sec. 10.4)

##### Simplicity

Records that serve no needed or significant purpose shall not be maintained. Excessive details and unnecessary refinements in accounting records shall be avoided. (Sec. 8.10)

## DISCUSSION

These principles and standards require that the amounts reported are the best possible estimate of the amounts which will ultimately be paid and the amounts reported represent valid obligations.

The agency must report obligation information promptly to allottees, suballottees, and any others within the agency that are responsible for the day-to-day control to assure that obligations and expenditures are restricted to authorized obligational authority. As a general rule, fund status reports should be provided as frequently and timely as necessary to preclude the necessity for maintaining cuff records.

## CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Are the types of fund control information to be provided to those responsible for the control of obligational authority described?	_____	_____
2. Is a sample format for each fund control report included, showing illustrative data elements, with pro forma data inserted?	_____	_____

## SUMMARY

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 7

### ACCOUNT STRUCTURE

### ACCOUNTS REQUIRED

#### OBJECTIVES

Our primary objectives are to ensure that the agency has:

- defined the entities to be served by the system and that they are appropriate,
- established appropriate accounts and records necessary to adequately record the specified information,
- provided for transactions to be recorded only once, and
- adopted a coding structure that complies with applicable principles and standards.

#### APPLICABLE PRINCIPLES AND STANDARDS

##### Structure of accounting system

The structure of the accounting system should be designed so that major assignments of responsibility or areas of activity can be readily reported on. (Sec. 8.5)

Each agency must clearly define the entities for which separate groups of accounts are to be established. (Sec. 11.1)

Transactions recorded in agency accounts should not be re-copied even in summary form in the accounts of agencies at higher organizational levels. Instead, financial reports submitted by subordinate levels should be utilized in preparing summary reports. Adequate provisions should be made for technical supervision and interlocking accounting relationships between offices to assure the validity of consolidated agency reports. (Sec. 8.7)

##### Basic accounts

Each accounting system shall provide complete and reliable records of the resources and operations of the entity to which it relates. Such records shall embrace all funds, property, and other assets, as well as liabilities and obligations, receipts and revenues, expenditures and costs. (Sec. 8.7)

Interagency and interfund transactions should be separately identified in agency records. (Sec. 8.7)

Accounts should be provided for assets, liabilities, investments of the U.S. Government, and others if applicable, and for revenues and costs. (Sec. 11.4)

The accounting system should provide classifications according to kinds of costs incurred. (Sec. 16.5)

#### Adequacy of accounts

The system ~~must~~ be capable of producing the financial information needed to:

- a. meet the reporting requirements of other Federal agencies, particularly the Office of Management and Budget and the Treasury Department,
- b. keep the Congress fully informed on the agency's operations and financial status, and
- c. provide such financial data as are required by law or by congressional committees. (Sec. 8.2)

All proper needs, internal and external, must be considered. (Sec. 8.4)

Agency accounts should be kept in such detail as is necessary to meet all management needs, including the furnishing of information needed by other agencies in the executive branch and by the Congress. (Sec. 8.7)

Accounting records should be maintained primarily in monetary terms, but quantitative data should be maintained as necessary or appropriate for producing useful information for management. (Sec. 8.7)

Each agency accounting system shall be designed to enable the prompt preparation of all needed financial reports. (Sec. 17.1)

Financial reports shall be based on official records maintained under an adequate accounting system that produces information objectively disclosing the financial aspects of all events or transactions taking place. (Sec. 17.3(a)(3))

### Coding requirements

Planning, programming, budgeting, and accounting classifications should be consistent with each other to the extent possible and synchronized with the agency's organization structure. (Sec. 8.6)

Each accounting system must provide appropriate fund identification of financial resources and transactions. (Sec. 11.2)

### DISCUSSION

The essence of these principles and standards is that the agency must structure its accounting operations so that each accounting system will provide current, complete and accurate financial information relative to the entities which it serves. (Assurance that a system does provide such financial information is a general objective of the accounting processes review section.)

The agency must establish the accounts needed to record specified types of financial information. These accounts must be established, when applicable, even if the agency has no plans to use the recorded information.

The agency must design its accounting system so that the financial and quantitative information needed to prepare financial reports and statements will be available from the accounts and records.

### CHECK LIST

	<u>Answer</u>	<u>References</u>
1. Does the design specify the locations and organizational levels at which accounts and supporting documentation will be maintained and at which accounting activities will be performed? (Sec. 27.5 3.e)	_____	_____
2. Where the accounting system is decentralized, does the design provide for compatible accounting between offices to assure the validity of consolidated agency reports?	_____	_____



	<u>Answer</u>	<u>Reference</u>
3. Is there a description of the coding structure which shows how financial data will:		
a. relate to the agency's organization structure?	_____	_____
b. relate to structure of internal operating budgets?	_____	_____
c. be consistent with classifications used in budget requests presented to the Congress?	_____	_____
d. meet object classification requirements of OMB?	_____	_____
e. provide fund and appropriation identification needed for reports to Treasury and OMB?	_____	_____
f. relate to the agency's programs or functions and cost centers?	_____	_____
4. Does the design include a listing of general ledger accounts by title and number? (Sec. 27.5 3.a)	_____	_____

#### SUMMARY

Describe briefly the basic structure of the accounts. (2/19/75 Memo, Item C(1)(c))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 8

### ACCOUNT STRUCTURE

### ACCOUNT QUALITIES

#### OBJECTIVES

Our primary objective is to ensure that the accounts proposed by the agency will result in the required disclosures.

#### APPLICABLE PRINCIPLES AND STANDARDS

##### Fund control requirements

Data on proposed expenditures may be accumulated in the accounting records before they become valid obligations; however, appropriate corrections must be made prior to reporting so that amounts included in reports represent valid obligations as defined by law. (Sec. 10.4)

The system should provide for appropriate recognition of apportionments of appropriations and for subdivisions of fund authorizations. (Sec. 10.6)

Subdivisions of fund authorizations for budgetary control purposes should be established at the highest practical level, be consistent with assignments of responsibility, and be limited in number to those necessary for effective control. (Sec. 10.6)

The system must provide for compliance with applicable limitations. (Sec. 10.7)

Appropriate accounts shall be maintained to provide a clear showing of the status of all appropriations in terms of apportionments, allotments, obligations, disbursements and collections, and accrued expenditures, revenues, and reimbursements. (Sec. 14.2)

##### Cost requirements

The cost accounting system should provide for the accumulation of information on all significant elements of cost and permit identification of the costs financed by the agency's appropriations and funds, as distinguished from other costs. (Sec. 16.4(1))

Accounting systems must provide for the systematic accumulation of cost information by:

1. major organizational segments,
2. budget activities, and
3. program structure.

The extent to which more detailed cost information by operational cost centers, projects, or units of work or end products should be accumulated must be determined by each agency, considering its operations and the uses to be made of the data in controlling and in evaluating the cost of performance by responsible officials. (Sec. 16.4)

Accounting systems should classify costs according to (1) acquisition of assets, and (2) current expenses. (Sec. 16.5)

The accounting system should provide classifications according to kinds of costs incurred. (Sec. 16.5)

Depreciation must be accounted for in specific circumstances. (Sec. 16.8(b))

#### Other requirements

Separate accounts for major categories of cash resources are to be established, with further subdivision to disclose important restrictions on availability for use. (Sec. 12.2(1)(D))

Separate accounts for major categories of receivables should be maintained. (Sec. 12.4(3))

Records shall be maintained of all transactions affecting the receivables. (Sec. 12.4(5))

Estimates shall be made of the portion of accounts receivable that may not be collectible. Such estimates shall be accounted for separately. (Sec. 12.4(6))

Significant classifications of property should be established to clearly disclose the nature of the property. (Sec. 12.5(c))

Property retired from service but not immediately disposed of should be classified separately to disclose its status. (Sec. 12.5(e))

Separate accounts for major categories of liabilities should be maintained. (Sec. 13.2(4))

The system shall provide for separate identification of funded and unfunded liabilities. (Sec. 13.2(4))

Appropriate records of contingent liabilities shall be maintained as part of the accounting system. (Sec. 13.3)

Accounts on Federal insurance, pension, and similar programs which are measured on an actuarial basis shall disclose the full current costs of these programs as they accrue and the estimated liability at any given time to make future payments. (Sec. 13.4)

The major elements of the Federal investment shall be separately accounted for. (Sec. 14.1)

Amounts borrowed from the U.S. Treasury shall be classified as part of the Federal investment until repaid or liquidated. (Sec. 14.3)

All realized gains or losses on exchange transactions shall be disclosed in agency accounts. (Sec. 16.8(f))

Separate accounts shall be maintained for unusual costs or losses of a nonrecurring nature which are substantial in amount. (Sec. 16.8(g))

#### DISCUSSION

These principles and standards require the agency to establish various accounts and records. Regarding fund control, the agency must maintain accounts which will disclose:

- the valid obligations incurred during a reporting period.
- the apportionments and subdivision of funds established for restricting obligations to amounts apportioned.

- the apportionments and subdivisions of funds.
- compliance with limitations.
- the status of each appropriation.

Regarding costs, the agency must maintain accounts which will disclose:

- current charges
- accumulated net income, if applicable
- costs by major organizational segment
- costs by budget activities
- costs by program structure
- costs of asset acquisitions
- depreciation and interest costs, under certain circumstances.

A discussion of the costs to be included in the accounts is included in Section 15 - Accounting for Costs.

#### CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design include a definition of each general ledger account by title and number? (Sec. 27.5 3.a)	_____	_____
2. Does the design include a list of subsidiary accounts to be maintained? (Sec. 27.5 3.c)	_____	_____
3. Are accounts provided for:		
a. major categories of cash resources?	_____	_____
b. major categories of receivables?	_____	_____
c. uncollectible accounts receivable?	_____	_____
d. significant classifications of property?	_____	_____

	<u>Answer</u>	<u>Reference</u>
e. advances and prepayments?	_____	_____
f. major categories of liabilities?	_____	_____
g. funded and unfunded liabilities?	_____	_____
h. contingent liabilities?	_____	_____
i. major elements of the Federal investment?	_____	_____
j. major categories of revenue?	_____	_____
4. Will accounts be maintained which will provide a clear showing of the status of all appropriations in terms of:		
a. apportionments?	_____	_____
b. allotments?	_____	_____
c. obligations?	_____	_____
d. disbursements and collections?	_____	_____
e. accrued expenditures?	_____	_____
f. revenues and reimbursements?	_____	_____
5. Will data on proposed expenditures be accumulated in accounting records before they become valid obligations?	_____	_____
a. if so, will appropriate corrections be made prior to reporting so that amounts shown on reports represent only valid obligations?	_____	_____
6. Are accounts maintained which will permit:		
a. accumulation of all significant elements of cost?	_____	_____
b. accumulation of costs by:		
(1) major organizational segment?	_____	_____
(2) budget activity?	_____	_____
(3) program structure?	_____	_____

	<u>Answer</u>	<u>Reference</u>
c. production of cost information by:		
(1) operational cost center?	_____	_____
(2) projects?	_____	_____
(3) units of work or end-products?	_____	_____
7. Do the accounts provide classifications according to kinds of costs incurred?	_____	_____
8. Are accounts included for:		
a. depreciation costs?	_____	_____
b. accumulation of depreciation?	_____	_____
9. Are accounts maintained to account for unusual costs or losses of a nonrecurring nature?	_____	_____
10. Will property retired from service but not immediately disposed of be classified separately?	_____	_____

#### SUMMARY

Describe briefly the account structure for allotments (and suballotments) and the cost (or accrued expenditure) account structure. (2/19/75 Memo, Item C(1)(c))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 9

### PROCESSES

#### GENERAL REQUIREMENTS

##### OBJECTIVES

Our primary objectives are to:

- identify the financial transactions which the agency will be required to account for on the accrual basis,
- ensure that the processes proposed by the agency will result in their recordation on the accrual basis, and
- ensure that the agency has devised accounting processes which will insure that only current, complete, accurate, and verifiable data are recorded in the accounts and records.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Accrual accounting

The maintenance of accounts on the accrual basis is required. (Sec. 9.1)

If the agency periodically converts accounting data recorded on the cash and obligation basis to the accrual basis, such conversions should be made not less frequently than monthly. (Sec. 9.1)

###### Accuracy and reliability

The system shall provide adequate documentary support for financial transactions. (Sec. 8.7)

Transactions should be recorded in a manner to provide a clear trail from source documents to summary records and to financial reports. (Sec. 8.7)

The highest standards of truthfulness and honesty must apply. Financial transactions shall not be recorded in the accounts in a manner that will produce inaccurate, false, or misleading information. (Sec. 8.9)



All transactions must be accounted for as realistically as possible and in accordance with the time and manner in which the events occurred. (Sec. 8.9)

All transactions occurring during an accounting period shall be recorded in the accounts for the period. (Sec. 8.10(b))

All financial data shall be accurate, reliable, and truthful. (Sec. 17.3(a)(2))

Financial reports prepared by Federal agencies must comply with the specific requirements of applicable laws and regulations as to accounting basis. (Sec. 17.3(b))

## DISCUSSION

The accrual basis of accounting is defined in Title 2 as "recognizing in the books and records of accounts the significant and accountable aspects of financial transactions or events as they occur." (2 GAO 9.1) Under this basis, the accounting system provides a current systematic record of changes in assets, liabilities, and sources of funds growing out of the incurrence of obligations, expenditures, and costs and expenses; the earning of revenues; the receipt and disbursement of cash; and other financial transactions.

These principles and standards require the agency to record only current, complete, accurate, and verifiable financial data in its accounts. The agency can best demonstrate compliance with these requirements by preparing complete flow charts of the principal accounting transactions. Complete flow charts identify (1) the action or event that initiates the process, (2) the methodology used to determine the amount, (3) the form or forms used to process the transactions, (4) the flow of the documents, (5) the function provided relative to the transaction by each organization involved in the process, (6) the location and nature of each internal control, and (7) the accounts or records to which financial data is posted.

## CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design describe the flow of documentary data through the principal accounting processes? (Sec. 27.5 4.a)	_____	_____
2. Is the application of the accrual basis of accounting described?	_____	_____

	<u>Answer</u>	<u>Reference</u>
3. Will the accounting system be maintained centrally using data provided to it by decentralized activities?	_____	_____
a. if so, does the design documentation demonstrate the controls which exist over the timeliness and accuracy of data provided by decentralized activities?	_____	_____

#### SUMMARY

Briefly comment on the application of the accrual basis of accounting in the system. (2/19/75 Memo, Item C(1)(a))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 10

### PROCESSES

#### ACCOUNTING FOR ASSETS OTHER THAN PROPERTY

##### OBJECTIVES

Our primary objectives are to determine:

--whether proposed procedures will result in the prompt, accurate, and complete recording of all applicable transactions.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Accounting for cash

Recording of disbursements should be on the basis of paid vouchers. However, if disbursing is performed by another agency, the disbursements may be recorded on an approved voucher basis, provided that the manner in which they are recorded facilitates reconciliation with the central accounting records of the Treasury Department. (Sec. 12.2(1)(B))

Agency accounting records for cash transactions shall be closed as of the end of periods for which reports are to be prepared and shall include all transactions consummated during those periods. (Sec. 12.2(1)(C))

There shall be compliance with all applicable requirements imposed externally for the handling of cash resources. (Sec. 12.2(2))

###### Accounting for foreign currency

Each agency must observe the procedures of the Treasury Department with respect to foreign currency. (Sec. 12.3)

###### Accounting for receivables

Receivables shall be recorded accurately and promptly on completion of the acts which entitle an agency to collect amounts owing it. (Sec. 12.4(1))

Amounts to be recorded shall consist of the amounts actually due. (Sec. 12.4(2))

Loans shall be accounted for as receivables only after the funds have been disbursed. (Loans authorized but not disbursed should be disclosed in explanatory notes to financial reports rather than as assets.) (Sec. 12.4(4))

#### Accounting for uncollectible debts

Estimates shall be made of the portion of accounts receivable that may not be collectible. (Sec. 12.4(6))

The handling of receivables determined uncollectible must conform to Comptroller General procedures (Title 4). (Sec. 12.4(6))

#### Accounting for advances

Advances and prepayments are to be recorded as assets. The accrued expenditure shall be recorded when performance occurs and the asset account reduced accordingly. (Sec. 12.6)

Advance payments to contractors not related to performance shall be accounted for as advances for materials and services to be received. (Sec. 13.6)

When materials or services are sold to other agencies and financed through the use of working fund advances, the advancing agency shall account for the amounts advanced as advances until the materials or services ordered are received. (Sec. 13.7)

Payments to grantees in advance of work performed shall be accounted for as advances of the grantor agencies until evidence of performance has been received from the agencies. (Sec. 14.8(c))

#### DISCUSSION

External requirements relating to handling of cash transactions are contained in Part V of the Treasury Fiscal Requirements Manual and Treasury Department Circular Nos. 92, 176, 937 and 1030.

Treasury Department regulations regarding foreign currency are contained in chapter 3200 of part II of the Treasury Fiscal Requirements Manual and Treasury Department Circular Nos. 108, 115, 125, 799, 830, and 937 (Supp. I).

The agency must adopt procedures which will result in recordation of appropriate amounts in the accounts as an allowance for uncollectible debts and recordation in the proper accounts when a bad debt is incurred. As a practical matter, we do not require the agencies to establish an allowance for uncollectible debts if they do not normally incur a material amount of bad debts. The procedures which the agency intends to adopt to estimate uncollectible debts must result in the establishment of appropriate amounts.

#### CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design show the flow of data through the accounting system for those transactions that affect the asset accounts? (Sec. 27.5 4.a)	_____	_____
2. Is there a description of the general ledger asset accounts to be maintained? (Sec. 27.5 3.b)	_____	_____
3. Do definitions for each general ledger asset account include the intended account content, control functions in respect to subsidiary ledgers and identification of contra accounts? (Sec. 27.5 3.b)	_____	_____
4. Is there a listing or an outline of accounts and records to be maintained which are subsidiary to the general ledger asset accounts? (Sec. 27.5 3.c)	_____	_____
5. Is there a description of the books of original entry and their functions in regards to the applicable general ledger and subsidiary accounts or records? (Sec. 27.5 3.d)	_____	_____
6. Does the design describe the process by which the following transactions will be recorded:		
a. cash receipts?	_____	_____
b. cash disbursements?	_____	_____

	<u>Answer</u>	<u>Reference</u>
c. the establishment of receivables?	_____	_____
d. liquidation of receivables?	_____	_____
e. advances and overpayments?	_____	_____
f. reduction of advances and prepayments?	_____	_____

SUMMARY

Briefly comment on \_\_\_\_\_ accountability for all assets  
(except property) with particular emphasis on cash and receivables.  
(2/19/75 Memo, Item C (1) (d))

## SECTION 11

### PROCESSES

#### ACCOUNTING FOR PROPERTY

##### OBJECTIVES

Our primary objectives are to:

- ensure that current, complete and accurate data are recorded in monetary and ~~quantitative~~ **property records** and that all related principles and standards are complied with,
- identify the capitalization criteria adopted by the agency and ensure that the procedures which the agency intends to adopt ~~comply~~ with it,
- determine whether the agency must account for depreciation and, if so, ensure that the procedures which the agency intends to adopt provide for appropriate consideration of each of the required factors, and
- ensure (1) that the procedures which the agency intends to adopt to control property while it is in inventory and to assign property to individuals for accountability purposes are appropriate and (2) that the agency has established a written policy which requires physical inventories to be conducted at reasonable intervals.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Accounting for property--general requirements

Each agency should adopt accounting policies appropriate for its property. (Sec. 12.5(c))

Each agency should establish, as an integral part of its accounting system, an adequate and reliable system of records and related procedures to provide a proper accounting for the Government's investment in the property for which the agency has management responsibility. (Sec. 12.5(c))

Property accounting must include appropriate procedures for the recording of all transactions affecting the agency's investment in property including acquisition, use, application, consumption, disposal, and retirement; and for the keeping of property records in terms of quantity and location. (Sec. 12.5(c)(1) and (2))

Property records should include the identification of excess property and its use, transfer, or disposal. (Sec. 12.5(c)(2))

Where title to grantee-acquired property vests in the Government, appropriate property records shall be established. (Sec. 16.8(c))

Adequate records shall be maintained for seized property or other property held in the custody of an agency but not owned. (Sec. 12.5(f))

Each agency's accounting system must include adequate monetary property accounting records. (Sec. 12.5(b))

Repair and maintenance costs incurred to keep property in satisfactory operating condition shall be accounted for as current operating costs. (Sec. 12.5(e))

The records used to account for property owned by others may be integrated with the financial accounting system in conformity with the principles prescribed for owned property. This procedure is not mandatory if effective control can be achieved by other means. (Sec. 12.5(f))

Accounting records shall be brought into agreement with the results of physical inventories. (Sec. 12.5(g))

Property received from other agencies without reimbursement shall be accounted for as an increase in the Federal investment. (Sec. 14.4)

#### Accounting for acquisition of property

The primary basis of accounting for property is cost to the agency responsible for its management. Where incurred costs are not measurable, or not known, reasonable estimates or alternative bases such as appraised values may be used. Where a basis other than cost is used, that basis should be adequately documented. (Sec. 12.5(c))



The basic cost of property shall include the amounts paid to acquire it, including transportation, installation, and related cost of obtaining the property in the form and place to be used or managed. (Sec. 12.5(d))

Easements and rights-of-way are included in the basic cost of property acquired. (Sec. 12.5(d))

Agency accounting policies should prescribe the accumulation of all significant costs applicable to property acquisitions. (Sec. 12.5(d))

Fixed assets shall be capitalized in accordance with capitalization criteria established as part of the agency's accounting policies. (Sec. 12.5(d))

Capitalization criteria should be defined in terms of identifiable units or groupings of property. In establishing identifiable units or groupings due consideration should be given to materiality. It is appropriate to establish reasonable dollar minimums as a basis for excluding certain property units from capitalization. No minimums in excess of \$300 should be established. (Sec. 12.5(d))

If current costs would be distorted in a given period by charging a large quantity of items which cost less than the minimum, such items should be recorded in a separate asset account and amortized over a reasonable period of time. (An example would be where a substantial amount of office furniture is purchased with a large portion involving items which individually cost less than the minimum.) The separate account established for the items which cost less than the minimum need not be supported by individual property records. (Sec. 12.5(d))

When assets are acquired by construction, accurate costs must be recorded and transferred to fiscal property accounts when work is completed. (Sec. 12.5(d))

Cost of facilities constructed by or for the Government should include all material elements of costs. (Sec. 12.5(d))

Interest costs incurred during construction should be capitalized. (Sec. 12.5(d))

Property acquired under installment contracts should be capitalized at the time of receipt or acceptance rather than periodically as payments are made or when title passes to the Government. (Sec. 12.5(d))

The amount capitalized for property acquired under installment contracts should include the purchase price plus related costs. (Related costs would include costs incurred for site preparation, installation, and similar costs related to making the equipment ready for use, which are incurred separately from the installment purchase contract or separately identified for payment in the contract.) These related costs should be capitalized when incurred. (Sec 12.5(d))

Property acquired under lease-purchase contracts should be capitalized at the time the option to purchase equipment is exercised and should include the purchase price under the contract less any accumulative allowances. Property acquired under lease purchases which are in fact installment purchases (the decision to purchase having already been made) will be treated for capitalization purposes as installment purchases. (Sec. 12.5(d))

Property transferred on a non-reimbursable basis shall be accounted for by the receiving agency at an estimated amount taking into consideration its usefulness to the agency, condition and market value. The receiving agency shall be advised by the transferring agency of the date and amount of accumulated depreciation. When the receiving agency's estimated amount differs from the depreciated cost reported by the transferring agency, the basis for establishing the value of the acquired property shall be clearly documented in the records. (Sec. 12.5(d))

Property transferred on a reimbursable basis shall be accounted for by the receiving agency at the transfer price but at not less than its estimated useful value. (Sec. 12.5(d))

Transportation, installation, and related costs incurred by the receiving agency shall be added to the accounting basis for property transferred. (Sec. 12.5(d))

Property acquired by trade-ins shall be recorded at the lesser of (1) the cash paid or payable, plus the amount allowed by the seller on the traded-in property, or (2) what the purchase price would have been had there been no trade-in. (Sec. 12.5(d))

The cost of property acquired by foreclosure shall be capitalized at the lesser of (1) the appraised (fair market) value or (2) the amount owed by the borrower plus any other costs incurred by the agency. (Sec. 12.5(d))

Property acquired by donation, devise, forfeiture or confiscation shall be recorded at an estimated amount representing what the Government would have been willing to pay for it, giving consideration to usefulness, condition, and estimated market value. (Sec. 12.5(d))

In determining the cost of purchase property, discounts shall be deducted from the prices billed. Purchase discounts are not income and shall not be accounted for as such. In determining the cost of purchase property, the amount to be recorded will be net of discount, whether or not the discount is taken. (Sec. 12.5(d))

Costs of handling and storage may be prorated as a part of the cost of materials and supplies before use or accounted for separately as operating costs. (Sec. 12.5(d))

The agency should determine whether to include handling and storage costs in the cost of property on the basis of possible benefits to be gained in the form of improved management control and administrative costs. (Sec. 12.5(d))

Late payment penalties are a cost of operations, and the amount of such loss shall be established in a separate account. (Sec. 12.5(d))

The cost of improvements which have an estimated useful life longer than one year and are made to leased properties, or to occupied properties owned by another Government agency, should be capitalized. (Such leasehold improvements would include carpeting, space partitions, soundproofing of ceilings and walls, and alterations. ) (Sec. 12.5(e))

Where the useful life of property has been extended or capacity to render service increased because of additions, replacements, betterments, alterations, or rehabilitations, the costs incurred shall be capitalized. (Sec. 12.5(e))

#### **Accounting for property disposal**

Materials and supplies issued for use shall be charged to using activities on the basis of cost, determined by the simplest method that produces reasonable and useful measures of cost. Acceptable methods include (1) specific identification of cost of items issued, (2) cost determined on first-in first-out assumption, (3) computed average cost, and (4) standard cost adjusted from time to time to reflect changes in actual cost. (Sec. 12.5(d))

Where the useful life of property has been extended or capacity to render service increased because of addition, replacements, betterments, alterations, or rehabilitation, the cost of features superseded or destroyed shall be removed from the property accounts. (Sec. 12.5(e))

The cost or other basis for accounting for property retired from service shall be removed from the accounts along with any accumulated depreciation. (Sec. 12.5(e))

Removal costs and amounts realized from sale, reimbursable transfer, or other salvage should be considered in determining the loss or gain on the retirement. (Sec. 12.5(e))

The book value of property transferred to other agencies without reimbursement shall be accounted for as a reduction of the Government's investment. (Sec. 12.5(e))

Property transferred to other agencies without reimbursement shall be accounted for as a reduction of the Federal investment. (Sec. 14.4)

#### Accounting for depreciation

Procedures shall be adopted by each agency to account for depreciation (or amortization of cost) of capital assets whenever a periodic determination of the cost of all resources consumed in performing services is needed. (Sec. 12.5(h))

Where depreciation is to be accounted for, agency accounting policies shall provide for writing off the costs of all capitalized assets acquired and used in performing services over the estimated period of their usefulness. (Sec. 12.5(h))

The amount to be written off shall be reduced by reasonable estimates of realizable salvage values at the end of the projected period of usefulness. (Sec. 12.5(h))

Leasehold improvements should be depreciated over the estimated period of occupancy or the life of the improvements, whichever is less. (Sec. 12.5(e))

#### Physical control of property

Each executive agency must maintain adequate inventory controls and accountability systems for its property. (Sec. 12.5(b))

Property accounting must include the making of independent checks on the accuracy of the accounting records through periodic physical count, weight, or other measurement. (Sec. 12.5(c)(3))

Physical inventories of both expendable materials and supplies and fixed assets shall be taken at regular intervals. (Sec. 12.5(g))

Differences between quantities determined by physical inspection and those shown in accounting records shall be investigated to determine causes of differences and identify necessary improvements in procedures to prevent errors, losses, or irregularities. (Sec. 12.5(g))

#### DISCUSSION

The above principles and standards prescribe, either specifically or generally, the criteria which the agency should follow when determining the amount at which property will be recorded in the accounts and records, as well as criteria for recording issued materials and supplies and released property.

The agency should indicate in the design how it plans to control the use, maintenance, and movement of its various types of property. For many types of property these controls probably will be outside the accounting system.

CHECK LIST

Answer      Reference

1. Does the design show the flow of data through the accounting system for those transactions that affect:

a. expendable property accounts?

\_\_\_\_\_

b. non-expendable property accounts?  
(Sec. 27.5 4a)

\_\_\_\_\_

2. Is there a description of the general ledger:

a. expendable property accounts?

\_\_\_\_\_

b. non-expendable property accounts?  
(Sec. 27.5 3.b)

\_\_\_\_\_

3. Is intended account content, control functions in respect to subsidiary ledgers and identification of contra accounts described for each:

a. expendable property account?

\_\_\_\_\_

b. non-expendable property account?  
(Sec. 27.5 3.b)

\_\_\_\_\_

4. Is there a listing or an outline of accounts and records to be maintained which are subsidiary to the general ledger:

a. expendable property accounts?

\_\_\_\_\_

b. non-expendable property accounts?  
(Sec. 27.5 3.c)

\_\_\_\_\_

	<u>Answer</u>	<u>Reference</u>
5. Is there a description of the books of original entry and their functions in regard to the applicable general ledger and subsidiary accounts or records? (Sec. 27.5 3.d)	_____	_____
6. Will property records be maintained in terms of quantity and location?	_____	_____
7. Will repair and maintenance costs applicable to property be accounted for as current operating costs?	_____	_____
8. Does the design documentation indicate that:		
a. physical inventories of fixed assets will be taken at regular intervals?	_____	_____
b. physical inventories of material and supplies will be taken at regular intervals?	_____	_____
c. accounting records will be brought into agreement with the results of physical inventories?	_____	_____

	<u>Answer</u>	<u>Reference</u>
d. differences between quantities determined by physical inspection and those shown in accounting records will be investigated:		
(1) to determine causes of differences?	_____	_____
(2) to identify necessary improvements in procedures to prevent errors, losses, and irregularities?	_____	_____
9. Does the design documentation explain the agency's capitalization criteria?	_____	_____
10. Does the design documentation describe the basis for determining and recording the amount of cost for the following types of property:		
a. fixed assets?	_____	_____
b. material and supplies?	_____	_____
c. property acquired by:		
(1) construction?	_____	_____
(2) lease-purchase contract?	_____	_____
(3) trade-in?	_____	_____
(4) foreclosure?	_____	_____
(5) devise?	_____	_____
(6) forfeiture?	_____	_____
(7) confiscation?	_____	_____
(8) donation?	_____	_____
(9) installment purchases?	_____	_____
d. property transferred on a:		
(1) reimbursable basis?	_____	_____
(2) nonreimbursable basis?	_____	_____
e. leasehold improvements?	_____	_____



	<u>Answer</u>	<u>Reference</u>
11. In determining the cost of purchased property will the amount to be recorded be net of discounts whether or not the discount is taken?	_____	_____
a. does the design show how purchase discounts and discounts lost will be accounted for?	_____	_____
12. Does the design documentation show that:		
a. the cost incurred in the following situations will be capitalized:		
(1) additions?	_____	_____
(2) replacements?	_____	_____
(3) betterments?	_____	_____
(4) alterations?	_____	_____
b. the cost of features superseded or destroyed in the above situations will be removed from the property accounts?	_____	_____
13. Will material and supplies issued for use be charged to activities on the basis of cost?	_____	_____
14. Upon retirement of property from service:		
a. will the cost of such property be removed from the accounts?	_____	_____
b. will the depreciation accumulated on such property be removed from the accounts?	_____	_____
c. will the loss or gain on retirement take into consideration:		
(1) removal costs?	_____	_____
(2) amounts realized from sale?	_____	_____
(3) other salvage?	_____	_____

	<u>Answer</u>	<u>Reference</u>
15. When property is transferred to other agencies without reimbursement, will the book value be accounted for as a reduction of the Government's investment?	_____	_____
16. Does the design documentation describe the process by which depreciation will be determined and recorded?	_____	_____
17. Will leasehold improvements be depreciated?	_____	_____

#### SUMMARY

Comment briefly on control over and accountability for property.  
(2/19/75 Memo, Item C(1)(d))

Comment on the criteria for capitalization of nonexpendable property. (2/19/75 Memo, Item C(1)(e))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 12

### PROCESSES

#### ACCOUNTING FOR LIABILITIES

##### OBJECTIVES

Our primary objectives are to determine:

- whether proposed procedures will result in current, complete, and accurate recording of all applicable transactions, and
- whether the accounting system needs to provide records of contingent liabilities and, if so, ensure that records of contingent liabilities are properly maintained.

##### APPLICABLE PRINCIPLES AND STANDARDS

Liabilities shall be measured and recorded in the period in which incurred. (Sec. 13.2(1))

Liabilities shall be removed from the accounts in the period that they are liquidated. (Sec. 13.2(1))

Amounts to be recorded as liabilities shall represent the amounts actually owed under contractual or other arrangements. (Sec. 13.2(2))

Accounting records shall be maintained so that all transactions relating to liabilities are included as of the end of the accounting period. (Sec. 13.5(5))

The purchase price included in installment or lease-purchase contracts, which are in substance installment purchases, shall be recorded as a liability when the property is received or accepted from the contractor. For lease-purchase contracts, the purchase price shall be recorded as a liability when the option to purchase is exercised. (Sec. 13.5)

Under contracts involving constructive delivery the liability to pay for work is incurred as it is performed by the contractors. The liability shall be recognized and recorded on the basis of reported performance of work. (Sec. 13.6)

Agencies shall separate funded from unfunded accrued annual leave liability in their revolving fund accounts. (Sec. 13.9)

When materials or services are sold to other agencies and financed through the use of working fund advances, the performing agency shall account for the amounts advanced as a liability until it has completed its performance. (Sec 13.7)

Amounts received in advance of performance should be accounted for as liabilities. (Sec. 15.8)

Appropriate records of contingent liabilities shall be maintained as part of the accounting system. (Sec. 13.3)

Incurred liabilities shall be accounted for and reported irrespective of whether funds are available or authorized for their payment. (Sec. 13.2(3))

#### DISCUSSION

Recording liabilities in the period in which incurred and removing them from the accounts in the period in which liquidated will result in full and proper disclosure of the agency's financial position in its financial reports.

Principles and standards relating to the liability for employees accrued annual leave are contained in the section relating to accounting for costs (Section 15 of this review guide).

Contingent liabilities are further discussed in Section 13.3.

#### CHECK LIST

1. Does the design show the flow of data through the accounting system for those transactions that affect the liability accounts? (Sec. 27.5 4.a)

Answer      Reference

\_\_\_\_\_

	<u>Answer</u>	<u>Reference</u>
2. Are the general ledger accounts for liabilities clearly described? (Description should define the account content, control function in respect to subsidiary ledgers, and identify each affected account.) (Sec. 27.5 3.b)	_____	_____
3. Is there a listing or an outline of accounts and records to be maintained which are subsidiary to the general ledger liability accounts? (Sec. 27.5 3.c)	_____	_____
4. Is there a description of the books of original entry and their functions in regard to the applicable general ledger and subsidiary accounts? (Sec. 27.5 3.d)	_____	_____
5. Are the methods to be used in determining the amounts of and accounting for each type of liability transaction clearly described?	_____	_____
6. Does the design show the flow of data applicable to the following types of transactions through the accounting processes:		
a. receipt of goods or services?	_____	_____
b. determination of Federal liability on some other basis?	_____	_____
c. payment of liabilities?	_____	_____
d. reduction of liabilities through adjustment, etc.?	_____	_____
7. Are the memorandum records to be maintained for contingent liabilities described?	_____	_____
8. Is an appropriate criteria prescribed for determining when a transaction or event creates a contingent liability and for determining when a contingent liability should be removed from the record?	_____	_____

	<u>Answer</u>	<u>Reference</u>
9. Are the methods for determining the liabilities required to be measured on an actuarial basis described?	_____	_____
10. Where the liability to pay for work is incurred as it is performed, rather than when deliveries are made, does the design indicate the methods used to determine the amounts of the accrued expenditures and the related liabilities (or reduction of advances) on the basis of performance?	_____	_____
11. Is there an explanation of the methods to be used to determine the amounts of and to record accrued annual leave transactions?	_____	_____
12. Does the design documentation state when a liability will be recorded for:		
a. Installment Contracts?	_____	_____
b. Lease-Purchase Contracts?	_____	_____

#### SUMMARY

Comment briefly on controls established for each type of liability. (2/19/75 Memo, Item C(1)(f))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

SECTION 13  
PROCESSES  
ACCOUNTING FOR THE INVESTMENT  
OF THE U.S. GOVERNMENT

OBJECTIVES

Our primary objectives are to ensure that:

- the procedures proposed by the agency will result in a current, complete, and accurate presentation of the Government's investment in the assets of the agency, and
- all applicable principles and standards are complied with.

APPLICABLE PRINCIPLES AND STANDARDS

Major elements of the Federal investment shall be separately accounted for. (Sec. 14.1)

Property and services received from other agencies without reimbursement shall be accounted for as an increase in the Federal investment in the assets of the agency. (Sec. 14.4)

Transfers of property to other agencies without reimbursement shall be accounted for as a reduction of the Federal investment. (Sec. 14.4)

Net income shall reflect all costs of operations and revenues earned during the reporting period with the exception of prior period adjustments. (Extraordinary items shall be shown separately from the results of ordinary items on the statement of operations.) (Sec. 14.6)

Direct charges to accumulated net income shall be restricted to such transactions as distributions of income to the U.S. Treasury and prior period adjustments. (Sec. 14.6)

## DISCUSSION

The investment of the U.S. Government in the assets of the agency consists of the residual equity of the Government after accounting for all known liabilities and investments or equities of others.

Accumulated net income (or loss) from operations is mainly applicable to revenue-producing business-type activities. Net income represents the excess of revenues from operations over applicable expenses (the opposite situation would represent a net loss).

## CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design show the flow of data through the accounting system for those transactions that affect the U.S. Government's investment account? (Sec. 27.5 4.a)	_____	_____
2. Is there a description of the books of original entry in which transactions affecting the investment of the U.S. Government will be recorded? (Sec. 27.5 3.d)	_____	_____
3. Is there a description of the general ledger accounts to be maintained for each of the major elements of the Federal investment? (Description should define the account content, control functions in respect to subsidiary ledgers, and identification of each affected account.) (Sec. 27.5 3.b)	_____	_____
4. Is there a listing or an outline of accounts and records to be maintained which are subsidiary to the general ledger Federal investment accounts? (Sec. 27.5 3.c)	_____	_____

## SUMMARY

Comment on any problem areas noted. (2/19/75 Memo, Item D)



## SECTION 14

### PROCESSES

#### ACCOUNTING FOR REVENUES

##### OBJECTIVES

Our primary objectives are to:

- identify and evaluate the agency accounting policy which establishes the point when revenues become realizable and are recorded as revenue earned.
- ensure that the procedures proposed by the agency will result in recording revenues in accordance with applicable principles and standards.

##### APPLICABLE PRINCIPLES AND STANDARDS

Agency accounting systems shall provide for recording revenue transactions in accounting records when earned. (Sec. 15.3)

Agency accounting policy should establish the point when revenues become realizable, with reasonable practicable certainty, in terms of valid claims against the person or organizations receiving the goods or services. (Sec. 15.3)

Amounts received in advance of performance should be accounted for as liabilities until revenues are earned on the basis of performance. (Sec. 15.3)

Agencies carrying on business-type activities should prepare statements of operations disclosing revenues and costs. (Sec. 17.2(b))

Applicable costs incurred to produce revenues from sales of materials or services should be compared or matched with the amount of such revenues in preparing financial reports on revenue-producing operations. (Sec. 17.2(b))

The accounting system should provide classifications according to the types of revenues earned. (Sec. 15.3)

##### DISCUSSION

Revenues represent the increase in assets (or decrease in liabilities) which result from operations. Revenues result from:

1. services performed by the Government.
2. goods and other tangible property delivered to purchasers, and
3. amounts becoming owed for which no current performance is required.

Accounting for revenue should provide records of:

1. the amounts to be collected or otherwise accounted for, and
2. the revenue-producing operations of the agency in support of financial reports.

Contingencies that might result in gains should not be recognized in the accounts since to do<sup>so</sup> would recognize revenue prior to its realization. Contingencies that might result in gains should be carefully explained in financial statements.

#### CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design show the flow of data through the accounting system for those transactions that affect the revenue accounts? (Sec. 27.5 4.a)	_____	_____
2. Are the general ledger accounts to be maintained for the major categories of revenues clearly described. (Description should define the account content, control functions in respect to subsidiary ledgers, and identify each affected account.) (Sec. 27.5 3.b)	_____	_____
3. Is there a listing or an outline of accounts and records to be maintained which are subsidiary to the general ledger revenue accounts? (Sec. 27.5 3.c)	_____	_____
4. Are the methods to be used for determining and recording the amounts of accrued revenue clearly explained?	_____	_____
5. Is there identification of the point when revenues become realizable and are recorded as revenue earned?	_____	_____
6. Is there a description of the books of original entry in which transactions affecting revenues will be recorded? (Sec. 27.5 3.d)	_____	_____

	<u>Answer</u>	<u>Reference</u>
7. Does the design contain charts and/or narrative descriptions to show the flow through the accounting processes of data applicable to:		
a. transactions constituting the earning of revenue?	_____	_____
b. billings?	_____	_____
c. collection transactions?	_____	_____
8. Does the design contain the format, including pro forma data, of each prescribed internal report?	_____	_____
9. Do the internal reports compare revenues earned with the cost of providing the services or products?	_____	_____

#### SUMMARY

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 15

### PROCESSES

#### ACCOUNTING FOR COSTS

##### OBJECTIVES

Our primary objectives are to assure that:

- all elements of cost are appropriately accounted for,
- needed cost information will be produced by the system, and
- cost accounting techniques adopted by the agency support cost-based budgets.

In addition, we will identify any cost-finding techniques to be used, determine whether each such technique to be used is justified, and identify data needed to perform the cost-finding technique.

##### APPLICABLE PRINCIPLES AND STANDARDS

###### Accounting for costs--general

Accounting for costs is essential for implementing cost-based budgets. (Sec. 16.4)

Accounting for costs is required where reimbursement for services performed is to be at cost or where sales prices are primarily based on cost. (Sec. 16.4)

Accounting for costs is also required where full recovery of cost from customers or users of services is a statutory requirement. (Sec. 16.4)

Agency accounting systems shall incorporate appropriate cost accounting techniques so that needed cost information will be produced for management and reporting purposes. (Sec. 16.4)

Cost accounting techniques should include, whenever appropriate and feasible, the production of quantity data relating to performance. (Sec. 16.4)

In specific circumstances (see Sec. 12.5(h)), depreciation should be accounted for. (Sec. 16.8(b))

Cost data must be reasonably reliable but unnecessary precision and refinement should be avoided. (Sec. 16.4(2))

Accounting practices for allocating indirect costs must be devised with care so as to avoid producing cost data that obscures the total costs for which responsible managers should be held accountable. (Sec. 16.4(3))

Agencies should accrue in their accounts the cost and related liability for accrued annual leave as of the close of each fiscal year, as a minimum. (Sec. 16.8(a))

Separate accounts shall be maintained for unusual costs or losses of a nonrecurring nature which are substantial in amount. (Sec. 16.8(g))

All realized gains and losses on exchange transactions shall be disclosed in agency accounts. Other losses which have been incurred or are expected to occur during the reporting period shall be separately accounted for. (Sec. 16.8(f))

Accounting procedures should be adopted by each agency to incorporate costs incurred by other agencies into its accounting system whenever periodic determinations of total costs of performance are needed and the amounts of the costs incurred and paid by other agencies are determined to be of significance in relation to the total costs of the agency, activity, or operation on which financial reports are being prepared. (Sec. 16.8(d))

Reasonable estimates of costs incurred and paid by other agencies should be based on information obtained from the performing agency. (Sec. 16.8(d))

Repair and maintenance costs incurred to keep property in satisfactory condition shall be accounted for as current operating costs. (Sec. 12.5(e))

#### Accounting for grants

Payments to grantees in advance of work performed shall be accounted for as advances of the grantor agencies until evidence of performance has been received from the grantees. (Sec. 16.8(c))

Payments to grantees as reimbursement for work performed or costs incurred shall be accounted for as reductions of liabilities to pay for such work or costs. (Sec. 16.8(c))

Payment under grants where no performance or reporting by grantees is required or where the payments are scheduled to correspond with performance shall be accounted for as liquidations of the obligations and as costs incurred. (Sec. 16.8(c))

Reports from grantees shall be required at reasonably frequent periods under advance or reimbursable grants to serve as the basis for accounting entries. (Estimates may be used for monthly reporting purposes, if necessary.) (Sec. 16.8(c))

Upon termination of a grant, unused and improperly applied funds shall be collected or adjusted pursuant to the terms of the grant. (Sec. 16.8(c))

Upon grant termination, the agency shall arrange for the disposition of Government-owned property. (Sec. 16.8(c))

#### Accounting for interest cost

For agency programs or activities financed by advances or borrowings from the Treasury on which interest is required by law to be paid, the interest costs incurred and paid shall be accounted for in the same manner as any other costs which are paid by the agency. (Sec. 16.8(e))

If the interest required to be paid by an agency is significantly less than the interest cost to the Treasury, the difference should be accounted for as an additional interest cost in accordance with the same principles as those applicable to agency programs to which significant interest costs apply but are not required by law to be paid. (Sec. 16.8(e))

Where there is no requirement to pay the interest costs on the Government's investment and an agency is engaged in the performance of services or sale of property outside the Government for revenues, a determination should be made as to the significance of such costs. If these costs are significant in relation to the financial results of operation otherwise determined, and when an interest factor is included in revenues obtained from sales made or services rendered, the interest costs should be included in the accounts or reflected in footnotes to the financial statements. (The basis for determining interest costs is described in 2 GAO 16.8(e)). (Sec. 16.8(e))

It is not necessary that agencies performing services or producing products mainly for use within the Government include interest in their accounts or disclose it as a cost in their financial statements. (Sec. 16.8(e))

Cost data for such activities used in making comparisons for purposes of management decisions should include an interest factor whether or not recorded in the accounts. (Sec. 16.8(e))

#### Use of cost-finding techniques

Cost data by program classification may be obtained by appropriate cost-analysis techniques where maintenance of detailed account classifications for this purpose would not be justified. (Sec. 16.4)

Cost-finding techniques may be used in lieu of detailed cost accounting procedures to obtain data needed for special purposes where it is more economical and satisfactory results are obtained. (Sec. 16.6)

#### DISCUSSION

"Cost" refers to the financial measure of resources consumed in accomplishing a specified purpose. Cost information provides a common financial denominator for the measurement and evaluation of efficiency and economy in terms of resources used in performance.

Congressional policy calls for the use of cost information in budgeting and in the management of operations.

The production and reporting of significant cost information is essential for effective financial management. It is needed in making meaningful comparisons and in keeping costs within limits established by law, regulation, or agency management policy.

Every expenditure should be considered as a cost of some essential planned activity. To facilitate comparison, as well as control, the classification of planned and actual cost must follow a like pattern.

The "costs" included in cost reports should ordinarily be applied costs. When full costs are not required, accrued expenditures may be used in lieu of costs under certain circumstances. When full costs are required, applied costs should be used and provision should be made for including indirect costs and unfunded costs.

Section 16 of Title 2 contains extensive discussion on the nature, importance and use of cost data. Other sections of this review guide contain principles and standards specifically relating to cost reports (Sections 4 and 5) and cost accounts (Section 8).

#### CHECK LIST

Answer      Reference

1. Is there a listing by title and number of the general ledger accounts used to control the accumulation and distribution of costs? (Sec. 27.5 3.a)

\_\_\_\_\_

	<u>Answer</u>	<u>Reference</u>
2. Is there a description of each general ledger account listed above, including the intended account content, control function in regard to subsidiary accounts and identification of each affected account? (Sec. 27.5 3.b)	_____	_____
3. Does the design contain a listing or an outline of the cost accounts to be maintained?	_____	_____
4. Is there a description of the books of original entry and their functions in regard to the agency's general ledger and subsidiary cost account structure? (Sec. 27.5 3.d)	_____	_____
5. Are charts included depicting the flow of documentary data through the cost accounting processes supplemented by sufficient descriptions to enable relating the actions charted to the accounting objectives, records, internal controls, and financial reporting requirements included in the design presentation? (Sec. 27.5 4.a)	_____	_____
6. Does the design describe the following:		
a. the role of cost accounting, in terms of resources consumed, whether funded or unfunded, in relation to the program and operation? (Sec. 27.5 5.a)	_____	_____
b. the degree of refinement of operational classifications for cost accounting purposes? (Sec. 27.5 5.b)	_____	_____
c. the rationale and criteria by which accrued expenditures for personal services, materials and supplies, equipment, and other purposes will be charged to operational classifications? (Sec. 27.5 5.c)	_____	_____
d. the role of cost centers or other accounts for allocating, charging, and accumulating costs? (Sec. 27.5 5.d)	_____	_____
(1) Does the design describe the methods used to allocate and distribute indirect cost to cost centers?	_____	_____



	<u>Answer</u>	<u>Reference</u>
e. an explanation of the coding structure used as a basis for distributing and summarizing costs by activity? (Sec. 27.5 5.e)	_____	_____
f. the extent of association of quantitative data with costs? (Sec. 27.5 5.f)	_____	_____
g. the relationship of the cost accounts to the agency's cost-based budgeting? (Sec. 27.5 5.g)	_____	_____
h. whether all elements of cost are included or only significant elements of cost?	_____	_____
i. what elements of funded or unfunded cost will be included and excluded?	_____	_____
j. will distinction be made between controllable and uncontrollable costs?	_____	_____
k. the areas where cost-finding techniques will be used in lieu of cost accounts? (Sec. 27.5 5.i)	_____	_____
l. the treatment of unfunded costs (including leave, depreciation, and costs paid by other Federal agencies)?	_____	_____
m. the treatment of interest costs?	_____	_____
7. Are the methods to be used in determining the amounts of and accounting for each element of cost explained? (Sec. 27.5 4.b)	_____	_____

#### SUMMARY

Describe briefly:

1. cost accounting for major organizational segments, budget activities, and programs. (2/19/75 Memo, Item C (1)(g))

2. treatment of unfunded costs including leave, depreciation, and costs paid by other Federal agencies. (2/19/75 Memo, Item C(1)(h))

3. accounting support for cost-based operating budgets. (2/19/75 Memo, Item C(1)(j))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 16

### PROCESSES

#### ACCOUNTING FOR ACCRUED EXPENDITURES

##### OBJECTIVES

Our primary objective is to insure that the methods to be used in determining and recording the amounts of and accounting for accrued expenditures are adequate.

##### APPLICABLE PRINCIPLES AND STANDARDS

Expenditures accrue regardless of when cash payments are made, of whether invoices have been rendered, or in some cases, of whether goods or other tangible property have been physically received. (Sec. 9.2)

The portion of any such expenditures which is unpaid at a given point in time is a liability. (Sec. 9.2)

The portion of payments made for which the expenditure has not accrued (such as advances) is an asset. (Sec. 9.2)

For items manufactured and services performed to the Government's specifications, agencies shall record such transactions in each accounting period, including holdbacks and requests for progress payments. (When an agency finds it impractical to record unbilled contractor performance, such as from performance reports, only documented transactions need be recorded.) (Sec. 9.2)

##### DISCUSSION

Accrued expenditures are the charges incurred during a given period requiring the provision of funds for:

1. goods and other tangible property received,
2. services performed by employees, contractors, grantees, lessors, and other payees, and

3. amounts becoming owed under programs for which no performance or current services are required (such as annuities, insurance claims, other benefit payments, and some cash grants),

An expenditure accrues when a buyer of goods or services receives them and thereby becomes committed to pay for them. When a contractor provides goods to the Government, which he holds himself available to sell to others, the expenditure accrues when physical delivery by the contractor and receipt by the Government takes place and title passes.

Where goods or equipment are manufactured to the Government's specifications, the Government's expenditures are considered to accrue based on constructive receipt of goods or other tangible property, rather than physical receipt or passing of title. That is, expenditures in some cases accrue in each accounting period when the contractor earns a portion of the contract price. Formal acceptance of the work by the Government is not the determining factor.

A GAO publication entitled "Frequently Asked Questions About Accrual Accounting In The Federal Government" presents a detailed discussion of the nature of and accounting for accrued expenditures. Office of Management and Budget Bulletin 68-10 provides information and instructions to Federal agencies regarding the accrual of expenditures. Familiarization with both of these documents would be beneficial to the reviewer during his evaluation.

#### CHECK LIST

	<u>Answer</u>	<u>Reference</u>
1. Does the design documentation show the flow of data through the principal accounting processes for the accrual of expenditures? (Sec. 27.5 4.a)	_____	_____
2. Does the design documentation indicate the methods used in determining and accounting for the amount of accrued expenditures for the following types of transactions:		
a. personal services performed by employees?	_____	_____
b. material and supplies?	_____	_____

	<u>Answer</u>	<u>Reference</u>
c. equipment, goods and other tangible property which is <u>not</u> manufactured to the Government's specifications?	_____	_____
d. equipment, goods and other tangible property which is manufactured to the Government's specifications?	_____	_____
(1) under these circumstances, will the expenditure be accrued in the same accounting periods as the contractor earns a portion of the contract price?	_____	_____
(2) if not, will such expenditures be accrued based on documented performance?	_____	_____
e. services performed by:		
(1) contractors?	_____	_____
(2) grantees?	_____	_____
(3) lessors?	_____	_____
(4) other payees?	_____	_____
f. amounts becoming owed under programs for which no performance or services are required?	_____	_____

#### SUMMARY

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## SECTION 17

### PROCESSES

### FUND CONTROL

#### OBJECTIVES

Our primary objective is to assure that the agency's procedures for control of funds complies with applicable principles and standards and with statutory requirements.

#### APPLICABLE PRINCIPLES AND STANDARDS

The system shall be designed to assure that the resources of each separate fund and appropriation are applied only to legally authorized purposes. (Sec. 8.1)

The system shall incorporate appropriate techniques to assist in achieving fund control. (Sec. 10.2)

Obligations will be identified with the applicable appropriation or fund at the time they are incurred. (Sec. 10.3)

Only those amounts meeting the criteria of section 1311 of the Supplemental Appropriation Act, 1955 (31 U.S.C. 200) will be recorded as obligations. (Sec. 10.4)

Statements of obligations furnished to Congress or to any of its committees shall include only amounts representing valid obligations as defined by section 1311 of the Supplemental Appropriations Act, 1955. (Sec. 10.4)

Data on proposed expenditures may be accumulated in the accounting records before they become valid obligations; however, appropriate corrections must be made prior to reporting so that amounts included in reports represent valid obligations as defined by law. (Sec. 10.4)

The system must provide for compliance with dollar limitations imposed by law. (Sec. 10.7)

Appropriate accounts shall be maintained on the accrual basis to provide a clear showing of the status of all appropriations in terms of apportionments, allotments, obligations, expenditures, revenues, and reimbursements. (Sec. 14.2)

Agency accounting procedures shall provide for appropriate recognition of apportionments and subdivisions of fund authorizations. (Sec. 10.6)

Agencies must also control funds in accordance with the Impoundment and Control Act of 1974 which prescribes guidelines and procedures for the establishment of reserves and other deferral of budget authority. (Sec. 10.1)

## DISCUSSION

Each agency is required by section 3679 of the Revised Statutes (the Antideficiency Act) to have a system of administrative control of funds approved by the Director of the Office of Management and Budget. The system of administrative control of funds approved by OMB should be included in or appended to the agency's statement of accounting principles and standards.

Such a system must restrict obligations or expenditures to the amounts appropriated, to the balances in the funds involved, to the amounts of the apportionment or reapportionments made for the current fiscal period, and to the amounts of administrative subdivisions thereof made to restrict obligations and expenditures to amounts authorized.

The term "fund control" refers to management control over the use of fund authorizations to insure that funds are used only for authorized purposes and obligations and expenditures do not exceed the amounts authorized.

The accounting system design should describe how officials incurring obligations have a basis for knowing whether funds are available and how the accounting system supports the management system for the administrative control of funds.

The fund control system must provide reasonable assurance that obligations will be properly authorized and that funds are available to support the incurring of these obligations.

Requirements relating to fund control reports and fund control accounts are presented in other segments of this guide (Sections 6 and 8).

## CHECK LIST

Answer      Reference

1. Does the design show the flow of data through the records--from source documents to reports--for the following types of transactions:  
(Sec. 27.5 4.a)

	<u>Answer</u>	<u>Reference</u>
a. appropriation of funds?	_____	_____
b. apportionment of appropriations?	_____	_____
c. allotment of funds?	_____	_____
d. incurrence of the obligation?	_____	_____
e. further subdivisions of funds?	_____	_____
f. liquidation of the obligation when goods and/or services are received?	_____	_____
g. adjustment of the amount of obligation?	_____	_____
h. disbursement of funds?	_____	_____
2. Are general ledger accounts maintained to provide fund control described? (De- scription should include the interred account content and identification of each affected account.) (Sec. 27.5 3.b)	_____	_____
3. Is there a listing or an outline of the accounts to be maintained which are sub- sidiary to the general ledger fund control accounts? (Sec. 27.5 3.c)	_____	_____
4. Are books of original entry and their functions in regard to the applicable general ledger and subsidiary accounts described? (Sec. 27.5 3.d)	_____	_____
5. Is there an explanation of the criteria to be applied to determine when a valid obli- gation is created?	_____	_____
6. Are source documents for obligations incurred identified with the applicable appropriation or fund?	_____	_____
7. Is the above identity maintained through the accounting processes to financial reports?	_____	_____
8. Does the design material demonstrate that the fund control system can provide reason- able assurance that obligations will be properly authorized and that funds are available to support the incurring of these obligations?	_____	_____



	<u>Answer</u>	<u>Reference</u>
9. Does the outline of controls provide for:		
a. approval of obligating documents?	_____	_____
b. review of vouchers, and related documents (including invoice, obligation authorization document, receiving report) prior to payment?	_____	_____
c. pre-validation of obligations?	_____	_____
d. planning and projections of obligations and expenditures to be incurred?	_____	_____
10. Does the design contain:		
a. for each internal report, the level to which the report will be distributed, and its frequency?	_____	_____
b. reports which compare planned obligations and expenditures against those actually incurred?	_____	_____
c. a listing by title and form number of each external report produced or partially produced by the system showing the status of appropriations and funds? (Sec. 27.5 2.d)	_____	_____
11. Has the system for administrative control of funds been approved by the Office of Management and Budget?	_____	_____
12. Does the design demonstrate that obligation and expenditure of amounts authorized will not be reserved or deferred without Congressional knowledge and approval?	_____	_____

#### SUMMARY

Describe briefly the system for the administrative control of funds. (2/19/75 Memo, Item C(1)(b))

Comment on any problem areas noted. (2/19/75 Memo, Item D)

## INTERNAL CONTROL

### OBJECTIVES

Our primary objectives are to confirm that procedures proposed by the agency provide adequate internal control to assure that:

- financial reports are accurate and reliable,
- assets are safeguarded,
- revenues are collected or properly accounted for,
- an adequate audit trail is provided, and
- adequate administrative procedures are provided to systematically examine disbursement and collection transactions prior to disbursement or deposit.
- handling of cash receipts will provide adequate control over cash at all times and will result in prompt deposit, and
- adequate control is provided for each type of asset, including control over write-offs and write-downs of assets.

### APPLICABLE PRINCIPLES AND STANDARDS

Responsibility for the performance of all duties necessary to carry out the functions for which the agency exists should be clearly defined and specifically assigned, and appropriate authority for such performance should be delegated. (Sec. 6(2))

Responsibility for assigned duties and functions should be appropriately segregated as between authorization, performance, keeping of records, custody of resources, and review. (Sec. 6(3))

A system of forward planning is needed for determining and justifying needs for financial, property and personnel resources. (Sec. 6(4))

An adequate system of authorization and record procedures must be devised. (Sec. 6(6))

The performance of all duties and functions should be under proper supervision. (Sec. 6(8))

All performance should be subject to adequate review under an effective internal audit program. (Sec. 6(8))

All funds, property, and other resources for which an agency is responsible should be appropriately safeguarded. (Sec. 6(12))

Effective procedures should be established for the preaudit and approval of vouchers before they are paid subject to the use of statistical sampling techniques authorized by 31 USC 82b-1. (Sec. 12.2(3)(B))

Appropriate records of all cash received shall be made immediately after receipts. (Sec. 12.2(1)(A))

Disbursements shall be recorded promptly in the accounting records. (Sec. 12.2(1)(B))

Procedures should be adopted to insure that cash receipts are deposited promptly. (Sec. 12.2(1)(A))

There shall be appropriate division of duties among officials and employees who have responsibility for handling cash and keeping records of cash transactions. (Sec. 12.2(3)(A))

There shall be an independent internal audit review into the effectiveness of the cash control system. (Sec. 12.2(3)(D))

Adequate controls should be established to prevent duplicate payments. (Sec. 12.2(3)(C))

Adequate control over expenditures is required; including, for example, procedures to assure that goods and services paid for are actually received and that quality, quantity and prices are in accordance with applicable contracts or authorizations. (Sec. 6 (11))

Accounting procedures should be devised to assist in assuring that the revenues applicable to the agency's operations or its assets are collected or otherwise accounted for. (Sec. 15.2)

All transactions shall be so recorded that they can be readily traced from the originating documents to summary records and to the financial reports issued. (Sec. 8.7)

Procedures must be adopted to assure that assets (1) are used properly and for only authorized purposes, (2) do not leave the possession of the Government except under proper authorization, and (3) are not disposed of without proper authorization. Adequate measures should be taken for their care and preservation. (Sec. 12.1)

Procedures must be adopted to assure that assets are not written off or written down without proper authorization. (Sec. 12.1)

The system must provide the basis for control over funds, property, and other assets. (Sec. 8.2)

#### DISCUSSION

This section is closely related to and should be used in conjunction with the ADP review guide.

Agency procedures should include adequate administrative procedures for systematically examining disbursement and collection transactions to verify their legality, propriety, and correctness at the point in time when any needed preventive or corrective action can be most effectively taken. This examination should be made prior to disbursement or deposit. Where a satisfactory examination cannot be completed prior to disbursement or deposit, any steps needed to complete the procedures should be taken at the earliest practicable time, so that effective corrective action can be taken. These agency responsibilities were included in a letter from the Comptroller General to the Heads of Federal Departments and Agencies dated August 1, 1969 (B-161457).

In accordance with 31 USC 82b-1, an agency head may prescribe the use of adequate and effective statistical sampling procedures in the examination and approval of disbursement vouchers for amounts of less than \$500.

CHECK LISTAnswerReference

1. Does the design describe the manner in which financial, manpower and property resources are controlled and safeguarded? (Sec. 27.5 7.a) \_\_\_\_\_
2. Does the control of resources include regular authorization, approval, documentation, recording, reconciling, reporting, and related accounting processes? (Sec. 27.5 7.a) \_\_\_\_\_
3. Does the design contain an outline of controls over quantity, timeliness, reliability and accuracy of inputs, processing, and outputs (whether for manual, automated, or mechanical systems)? (Sec. 27.5 7.b) \_\_\_\_\_
4. Does the outline of controls sufficiently demonstrate reasonable assurance of accurate recording of transactions and reporting their effects in the accounting period in which they occur? (Sec. 27.5 7.b) \_\_\_\_\_
5. Have audit trails throughout the system been identified and described in the system design? (Sec. 27.5 7.c) The audit trail is the manner in which a particular element of data that exists in the files can be traced backward to the source of the transaction that created it and forward to its **position in a report.** \_\_\_\_\_
6. Does the design provide for examination (preaudit) of disbursement transactions prior to disbursement? \_\_\_\_\_
7. If disbursement transactions will not be examined prior to disbursement, does the design documentation indicate:
  - a. the point in time when such transactions will be examined? \_\_\_\_\_
  - b. why such transactions will not be examined prior to disbursement? \_\_\_\_\_

	<u>Answer</u>	<u>Reference</u>
8. Will statistical sampling procedures be used in the examination of disbursements for amounts of less than \$500?	_____	_____
9. Will such examination include review of vouchers and related documents (including invoices, obligation authorization documents, and receiving reports) in order to verify the legality, propriety and correctness of disbursement transactions?	_____	_____
10. Does the design documentation provide for examining collection transactions prior to collections being deposited?	_____	_____
11. If collection transactions will not be examined prior to deposit, does the design documentation indicate:		
a. the point in time when such transactions will be examined?	_____	_____
b. why such transactions will not be examined prior to deposit?	_____	_____
12. Will such examination include review of collections in order to verify their legality, propriety, and correctness?	_____	_____
13. Does the design documentation describe the controls established to prevent duplicate payments?	_____	_____
14. Does the design documentation describe control procedures established over assets other than cash?	_____	_____
15. Does the design documentation describe procedures established for handling cash?	_____	_____
16. Will proper authorization be required before assets are written off or written down?	_____	_____

	<u>Answer</u>	<u>Reference</u>
17. For records comprising the audit trails of the system, are retention periods specified?	_____	_____
a. Are these retention periods in accordance with the provisions of 8 GAO 9 and 8 GAO 10?	_____	_____
18. For automated systems, does the design documentation describe the:		
a. Controls over the data forwarded to the computer center for processing?	_____	_____
b. Controls over the output products forwarded from the computer center to the various accounting offices?	_____	_____
19. When edit and error listings are printed out for manual research and correction, does the design documentation describe controls to ensure that all items printed out are re-entered into the system?	_____	_____

#### SUMMARY

Describe briefly the internal controls planned for the system.  
(2/19/75 Memo, Item C(i))

Comment on any problem areas noted. (2/19/75 Memo. Item D)